

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: Banking and Insurance Committee

BILL: PCS/SB 1486

SPONSOR: Banking and Insurance Committee and Senator Garcia

SUBJECT: Property Insurance

DATE: March 4, 2005

REVISED: _____

ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1. Deffenbaugh	Deffenbaugh	BI	Pre-meeting
2. _____	_____	JU	_____
3. _____	_____	GA	_____
4. _____	_____	WM	_____
5. _____	_____	RC	_____
6. _____	_____	_____	_____

I. Summary:

Legislation enacted in the 2004 Special Session A requires that for residential property insurance policies issued or renewed on or after May 1, 2005, the hurricane deductible must be applied on an annual basis to all hurricanes that occur during the calendar year, rather than to each hurricane. This requirement applies to both personal lines residential policies (homeowners, mobile homeowners, etc.) and commercial residential policies (condominium associations, apartment buildings, etc.). Although the premium impact on homeowners and other personal lines policies is expected to be small (about 1 to 3 percent), it is likely to be much greater for condominium association policies.

The bill provides that the annual hurricane deductible requirement would be limited to personal lines policies and would not apply to commercial policies. However, for commercial residential policies issued or renewed on or after January 1, 2006, the insurer would be required to offer the policyholder the option of: 1) a hurricane deductible that applies on an annual basis (as required for personal lines policies), and 2) a hurricane deductible that applies to each hurricane.

The provisions of the bill are consistent with recommendations on this issue in the Final Report and Recommendations of the Joint Select Committee on Hurricane Insurance (February 28, 2005), appointed by the Senate President and Speaker of the House on January 5, 2005.

This bill substantially amends s. 627.701 of the Florida Statutes.

II. Present Situation:

Hurricane Deductibles; Special Session 2004-A

Legislation was enacted in the 2004 Special Session A related to hurricane deductible provisions of residential property insurance policies.¹ The legislation was in response to the financial impact on policyholders whose homes were damaged by two or more hurricanes and who were forced to absorb the cost of multiple deductibles. The legislation created a program to reimburse policyholders for part of this expense and required that future policies apply the hurricane deductible on an annual basis, to all hurricanes that occur during the calendar year.

Section 627.701, F.S., establishes the maximum and minimum hurricane deductibles that are allowable and mandates that insurers offer hurricane deductibles of specified amounts. The Legislature first authorized the use of separate, percentage hurricane deductibles for residential policies in 1993 after Hurricane Andrew. The Legislature's purpose in allowing for higher hurricane deductibles, as expressed in this statute, is to limit premium increases and to increase the availability of hurricane property insurance in Florida.

The law requires insurers to offer homeowners a 2 percent hurricane deductible, but for homes valued under \$100,000, the insurer must also offer a \$500 hurricane deductible, with certain exceptions. Based on reports filed by insurers with the Florida Hurricane Catastrophe Fund, about 76 percent of the homes in Florida have a hurricane deductible equal to 2 percent of the insured value of the dwelling. For a home insured for \$200,000, this means the first \$4,000 of hurricane damage is borne by the policyholder. About 16 percent of the homes in Florida have a deductible of \$500 or less. For homes valued at \$100,000 or greater, insurers generally do not offer a hurricane deductible lower than 2 percent, but some insurers do so. The maximum allowable deductible is 5 percent of policy limits, except for homes valued in excess of \$500,000 for which no maximum limit applies. About 5 percent of the homes in Florida have a 5 percent deductible.

Until the 2004 hurricane season, the Legislature had not fully considered the impact of multiple hurricanes damaging the same home in a single year. Deductibles in property and casualty insurance policies have historically applied to each covered event or occurrence. After four major hurricanes hit the state in August and September of last year, at least 30,000 policyholders were estimated by the Office of Insurance Regulation as having damage from two or more hurricanes and their deductible applied to each storm. However, in many other cases of multiple storm damage, insurers waived the application of multiple deductibles.

The Special Session act ("act") appropriated up to \$150 million from the Florida Hurricane Catastrophe Fund for the Department of Financial Services to reimburse residential policyholders whose property was damaged by two or more hurricanes and whose insurer applied more than one hurricane deductible. The act also amended s. 627.701, F.S., to require that residential property insurance policies apply the hurricane deductible on an annual basis to

¹ Chapter 2004-480, Laws of Fla. (House Bill 9-A), signed by the Governor on December 21, 2004.

all hurricanes that occur during the calendar year, rather than on a per-event basis. For example, if a home is insured for \$200,000 and has a 2 percent hurricane deductible, which is a \$4,000 hurricane deductible, it will apply to all hurricane losses for the year, rather than to each hurricane loss. However, insurers are allowed to apply the “other perils” deductible, which is typically \$500, or the remaining amount of the hurricane deductible, whichever is greater, to a loss for a second hurricane and each subsequent hurricane that year. Section 5 of the act (not codified in the Florida Statutes) provided that the amendments to s. 627.701, F.S., applied to policies issued or renewed on or after May 1, 2005. However, Section 5 made an incorrect cross-reference to the amendments to s. 627.701, F.S., made by “section 3” of the act, rather than the correct reference to “section 4.”

The annual deductible requirement applies to any *residential property insurance policy*. This term is interpreted as having the same meaning as *residential coverage*, as defined in s. 627.4025, F.S., which includes both *personal lines residential coverage* provided by homeowners, mobile home owners dwelling, tenants, condominium unit owners, cooperative unit owners and similar policies, and *commercial lines residential coverage* provided by condominium association, cooperative association, apartment building, and similar policies, including policies covering the common elements of a homeowners’ association.

As noted, the annual deductible requirement applies to policies issued or renewed on or after May 1, 2005. But, insurers are required by s. 627.4133, F.S., to give residential property insurance policyholders at least 45 days notice of the renewal premium, and at least 90 days notice prior to the effective date of nonrenewal or cancellation. Changes in policy forms and rates are subject to approval by the Office of Insurance Regulation.

Based on information provided by insurers and model loss estimates from the Florida Hurricane Catastrophe Fund, it was estimated that premiums may increase by about 1 to 3 percent due to the requirement for an annual hurricane deductible, assuming the same percentage deductible is applied. However, this estimate was based on the impact on homeowners policies and other personal lines residential policies. Representatives of insurers selling condominium association policies stated that the premium increase would be much greater for these policies, due primarily to its projected costs for additional reinsurance the insurers need to cover their increased exposure, and that premium increases may be 37.5 percent. The Office of Insurance Regulation also stated that the premium impact of the annual hurricane deductible for condominium association policies is likely to be greater than for homeowners generally, and may be in the 10 to 20 percent range. Insurance company representatives also stated that significant premium increases could probably be avoided by changing the deductible on a condominium association policy from a 2 percent (per event) deductible to a 3 percent annual deductible, which is permissible under the current law. But, this would mean that the condominium association would be subject to a greater deductible expense (3 percent rather than 2 percent of the policy limits), for each hurricane loss. Another possibility is that the insurer may be required to non-renew some policies if adequate reinsurance or capitalization cannot be obtained. Due to the 45-day notice requirement, premium renewal notices will begin to be mailed on about March 15, 2005, for policies that renew on May 1, 2005, and thereafter, that are subject to the annual deductible requirement.

Joint Select Committee on Hurricane Insurance

On January 5, 2005, Senate President Tom Lee and House Speaker Allan Bense appointed the Joint Select Committee on Hurricane Insurance (Committee). The Committee was directed to study all aspects of the property insurance market that promote the availability and affordability of coverage and to focus on three areas of immediate importance. The first area was hurricane deductibles, including the premium impact of the annual hurricane deductible requirement enacted in the 2004 Special Session A. The Committee held five meetings and issued its final report and recommendations on February 28, 2005. On the issue of the annual hurricane deductible, the report made the following findings and recommendations²:

The annual hurricane deductible is mandated -- it cannot be offered as an option to a deductible that applies to each hurricane. The Committee considered a proposal that insurers be required to offer both an annual and per event hurricane deductible, in order to provide a choice to a consumer. But, if the premium difference is minimal, it may be preferable to minimize confusion for policyholders and insurers alike, and assure that no policyholder will face the significant, unexpected expense of paying for two or more full hurricane deductibles. Information provided to the committee was consistent with earlier estimates that the premium impact of an annual hurricane deductible for homeowners is likely to be between 1 and 3 percent. Insurers are currently preparing forms and rates to file for approval with OIR to meet the law's requirement to apply the annual deductible to policies issued on or after May 1, 2005. Changing the law to require insurers to offer both an annual and a per event deductible at this time would be disruptive to the insurance market and of questionable benefit to consumers.

However, for condominium associations and other commercial residential policies, the premium impact of the annual hurricane deductible is likely to be greater than for homeowners generally. The committee cannot verify the accuracy of these estimates, but information provided to the committee indicates that the premium increases for such policies could be significant or result in an insurer offering a higher percentage deductible (such as 3 percent rather than 2 percent) in order to maintain the current premium level. This provides a much stronger argument for requiring insurers to offer commercial residential policyholders both an annual hurricane deductible and a per-event deductible as options.

Based on the above findings the Committee made the following recommendations:

1. *Retain the mandatory annual hurricane deductible for homeowners policies and other personal lines residential policies, rather than making the annual deductible an option for such policies.*
2. *Require insurers to offer both an annual hurricane deductible and a per event deductible to condominium associations and other commercial residential policies.*

² *Final Report and Recommendations of the Joint Select Committee on Hurricane Insurance* (Feb. 28, 2005); pp. 3 and 20; available at: <http://www.flSenate.gov/data/committees/joint/jsfi/finalreport.pdf>

III. Effect of Proposed Changes:

The proposed committee substitute would amend s. 627.701, F.S., to limit the application of the requirement that hurricane deductibles apply on an annual basis to *personal lines* residential policies. This includes homeowners, mobile home owners, dwelling, tenants, condominium unit owners, cooperative unit owners and similar policies. The proposed bill also clarifies that this requirement applies to policies issued or renewed on or after May 1, 2005 (the same date provided in the Special Session act, but which had an incorrect cross-reference.)

For *commercial lines residential policies*, the PCS would, instead, require insurers to offer the policyholder the option of: 1) a hurricane deductible that applies on an annual basis (as required for personal lines policies), and 2) a hurricane deductible that applies to each hurricane. This requirement would apply to policies for condominium associations, cooperative associations, apartment buildings, and similar policies, including policies covering the common elements of a homeowners' association. This requirement would apply to commercial residential policies issued or renewed on or after January 1, 2006.

The bill is effective upon becoming law, which would be the date it is signed by the Governor, or 7 days after presentation to the Governor unless it is vetoed.³ If the bill becomes law prior to May 1, 2005, it would supersede, for commercial policies, the current requirement that residential policies issued or renewed after that date have an annual hurricane deductible. However, due to the 45-day notice requirement, insurers will begin issuing premium renewal notices about March 15, 2005, for policies with a May 1 effective date. So, unless the bill becomes law by about March 15, some commercial policies may still be affected by the current law, depending on the actions taken by their insurer

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

³ FLA. CONST., Art. III, Sec. 8. (If during the 7-day period the Legislature adjourns sine die or takes a recess of more than 30 days, the Governor has 15 days to act on the bill.)

B. Private Sector Impact:

The bill would prevent potentially significant premium increases or increases in the percentage amount of the deductible for condominium associations and other commercial residential policyholders, due to exempting such policies from the annual hurricane deductible requirement. However, insurers would be required to offer both an annual deductible and a per event deductible to commercial policyholders, for policies issued or renewed after January 1, 2006. The policyholder would determine whether the increased premium for the annual deductible is worth reducing the risk of loss (deductible expense) due to multiple hurricanes.

Some commercial residential policies are written for small apartments for which the premium impact of an annual hurricane deductible is likely to be similar to homeowners and other personal lines residential policies, i.e., about 1 to 3 percent. For those policies, the proposed bill would require insurers to offer both an annual and per event deductible, at a minimal difference in premium, so the benefit to policyholders is limited.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Summary of Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
